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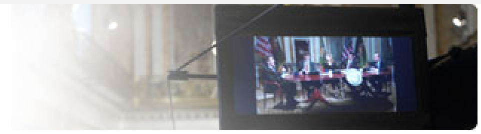

Testimony of Secretary Jacob J. Lew before the House Financial Services Committee

12/12/2013 **WASHINGTON** - Chairman Hensarling, Ranking Member Waters, and members of the committee, thank you for the opportunity to testify today.

There are signs that economic conditions are improving in most advanced economies, led by the United States. Despite political headwinds, our economy has been steadily growing. Over the past 45 months, our businesses have created more than 8 million jobs. While we are moving in the right direction, we have more to do to create jobs, accelerate growth and put our economy on a firmer foundation.

Progress at home in part depends on the state of a global economy that continues to face many challenges. The long recession in the euro area seems to be ending, although unemployment remains very high in many countries. Having made significant progress on achieving financial stability, Europe is now in a position to place greater priority on boosting demand and employment. In Japan, the central bank and parliament have taken forceful action to begin ending deflation, but to achieve sustained success Japan needs to undertake structural reforms to strengthen domestic demand growth. Recently, some emerging markets have slowed as post-crisis stimulus wanes. There has long been recognition that macroeconomic policy in the United States and other advanced economies will eventually return to normal as growth strengthens. Emerging markets need to make reforms that increase their resilience and address structural constraints to growth. China's new leadership recently announced bold commitments to reform. The pace and character of these reforms will shape China's economic transition toward domestic consumption led growth, and away from resource-intensive export growth.

Part of my job is to work to create the most favorable external environment for U.S. jobs and businesses. The international financial institutions – the International Monetary Fund (IMF) and multilateral development banks (MDBs) – are indispensable partners in this effort and it is imperative that we preserve our leadership in these institutions. Our investments in these institutions foster a more stable and vibrant global economy, which is critical to a growing U.S. economy. That is why it is so important that Congress acts to approve IMF quota and governance reform. At the G-20 Seoul Summit in 2010, we secured reforms that preserve the U.S. veto without increasing the U.S. financial commitment to the IMF. To implement these important reforms, the Administration has provided draft legislation to reduce U.S. participation in the New Arrangements to Borrow (NAB) and simultaneously increase the size of the U.S. quota in the IMF. This proposal will advance vital institutional reforms to modernize the IMF and preserve America's leadership role in the Fund.

The IMF anchors global financial stability

Since it was founded nearly 70 years ago, the IMF has been instrumental in securing U.S. economic interests by helping to maintain and restore economic and financial stability abroad. In response to the 2008-2009 global financial crises, the IMF once again was the first responder. Through its lending programs and policy advice, the IMF played a forceful role in mitigating the impact of the global crisis on its member countries to help prevent contagion. At the G-20 Summit in April 2009, the G-20 leaders mobilized $750 billion in increased resources for the IMF that stemmed capital outflows from emerging markets and stabilized the international financial system.

Notably, the IMF has played a critical role in helping Europe restore financial stability. While Europe has shouldered the lion's share of the financial support to EU member countries, the IMF has provided much-needed expertise and credibility. This has yielded tangible results, even though challenges remain. The IMF's role in stabilizing the economies in Europe has helped limit the negative effects of the crisis on the global economy and on the United States. As you know, the United States has an important stake in Europe's recovery and strength. For example, the European Union accounts for more than 20 percent of U.S. exports. Furthermore, more than 60 percent of foreign direct investment in the United States comes from EU companies, and these investments create jobs for American workers. Further, greater stability in financial markets in Europe helps to reduce the risks of volatility in U.S. markets, safeguarding American household savings and retirement accounts.

Although Europe remains our major trading partner, U.S. companies are increasingly looking to export their products to emerging markets. Because growth has slowed in some emerging markets, the IMF is advising governments to improve their policy frameworks and build greater resilience, including through exchange rate flexibility, supportive monetary policies consistent with inflation dynamics, and strengthened regulatory and supervisory policies.

The IMF is also an important partner for the United States as we seek to strengthen our national security in a rapidly changing world. Across the Middle East and North Africa, the IMF is supporting countries undergoing difficult economic transitions. The IMF has provided policy advice and technical assistance to countries in the region, along with financial support to Jordan, Morocco, and Tunisia. This work is far from done.

Our investment in the IMF is safe and smart. When the IMF lends, it does so subject to appropriate conditions and with safeguards to assure it is repaid. And its repayment record is outstanding. When the IMF draws on U.S. resources, we earn interest. The United States is exposed to the IMF's balance sheet – not to the borrowing countries – and the IMF's balance sheet is rock solid. The IMF is regarded as the world's preferred creditor, meaning that the IMF's member countries acknowledge and agree that it gets repaid first. And the IMF leverages U.S. resources – every dollar of financing from the United States is matched with more than four more from other countries around the globe.

Under the international agreement to implement the 2010 quota reforms, once Congress acts, the U.S. quota in the IMF will increase by approximately $63 billion, and the U.S. commitment to the NAB will decrease by an equal amount. Our overall commitment to the IMF will thus remain unchanged.

The 2010 quota and governance reforms are a good deal for the United States and the global economy. Without these reforms, we risk a loss of U.S. influence in the IMF as other countries seek to enhance their stature outside of the IMF's quota-based financial and governance structures. The 2010 agreement also facilitates changes in the composition of the IMF Executive Board, while preserving the U.S. board seat and veto power. That is why it is imperative that Congress act on IMF quota and governance reform as quickly as possible.

Today, U.S. approval is the only remaining step needed for these important reforms to go into effect. I look forward to working with you and your colleagues to get our proposal enacted quickly.

Raising financial regulation standards globally

Not only did the global financial crisis remind us why we need a strong IMF, it underscored the need for strengthening financial sector regulation across the globe. In particular, the crisis highlighted the need for building much stronger and more resilient financial institutions, greater market transparency, and a high quality level playing field across borders that protects against regulatory gaps, arbitrage, and a race to the bottom.

Building on the Dodd-Frank Act and in order to ensure that the world's standards were as high as our own, the United States led the G-20 to upgrade the Financial Stability Board's oversight role in financial regulation and to establish an ambitious agenda for international financial regulatory reform.

Due to the efforts of U.S. leadership, the G-20, and the Financial Stability Board, financial institutions are now well on their way to building significantly stronger, high-quality capital and liquidity buffers through Basel III. Leverage has been reduced. The CFTC's efforts have in considerable parts tackled the problem of an opaque OTC derivatives market. The FDIC is playing a leading global role in promoting international progress to address cross border resolution. At the same time, shadow banking is being addressed, the perimeter of regulation expanded, and systemically significant institutions are being designated for heightened supervision. Through the IMF and the World Bank's Financial Sector Assessment Program, as well as the FSB peer review process, the United States is working to promote consistent implementation of high-quality regulations across the globe to keep risk from migrating where regulation is weak.

While many of the core reforms of Dodd-Frank are largely completed at home, we have not yet completed the global regulatory race to the top. In 2014, the United States intends to focus our financial regulatory reform efforts in the G-20 and through the FSB on consistent international implementation. We will focus on promoting vigorous implementation of Basel III, ensuring that risk weighted assets are assessed consistently across borders, and that Basel III's high quality capital standard is met. We will encourage swift implementation of convergent clearing, trading, and reporting requirements for OTC derivatives markets. We will also focus on strengthening arrangements to facilitate the cross-border resolution of a large, complex financial institution, building on the FDIC's work. And we will work with our international partners to develop and implement a roadmap for strengthened and comprehensive oversight and regulation in order to address the systemic risks posed by shadow banking.

The multilateral development banks advance U.S. interests

Finally, let me turn to the role of the MDBs. At a time when the United States is striving to shape the global economy, the MDBs are important partners in supporting our national security objectives, promoting economic growth, and addressing global challenges. These institutions leverage our resources and multiply our impact by ensuring that other nations are contributing their share.

For example, in Afghanistan and Pakistan, the MDBs are working with local authorities to reduce poverty and build stronger institutions. In emerging economies, the MDBs are promoting economic reforms consistent with our values and interests. Take for example, the World Bank's annual Doing Business Report. This flagship publication, which ranks countries based on the strength of their investment climates, has spurred many countries to improve laws and regulations to attract private capital.

The MDBs are making long-term investments to help foster the next generation of emerging markets. Fast growing African countries present new opportunities for U.S. businesses. For example, we have worked successfully to secure support from the World Bank and the African Development Bank for President Obama's Power Africa Initiative, which aims to bring energy to half a billion people in Sub-Saharan Africa. The MDBs are playing a vital role in this effort, employing their resources and technical expertise to promote the difficult, yet crucial, reforms needed to encourage private sector investment in Africa's energy sector.

We rely on the MDBs to be global standard setters. For example, we are successfully raising the bar to minimize social and environmental risks associated with large infrastructure projects so that development is sustainable and broadly shared.

The MDBs are also central to our efforts to combat major global challenges that require multi-country solutions, including climate change and food insecurity. It is important to recognize that the gains in development over the last several decades are increasingly at risk due to the impacts of climate change, particularly in many of the poorest countries in the world. The Climate Investment Funds help those countries, where climate change is expected to have a disproportionate impact, become more resilient. Examples include a coastal embankment improvement project in Bangladesh and water resources mobilization in Niger. The Bangladesh project is helping reduce disaster risk for more than 700,000 people. The Niger project is helping bring water resources to individuals and farmers, which also is improving the lives of more than 700,000 people.

In 2009, President Obama committed U.S. support to confront the urgent challenge that 842 million people around the world face every day — the injustice of chronic hunger and malnutrition and the need for long-term food security. Treasury has successfully worked with the World Bank to mobilize more than $1 billion for the Global Agriculture and Food Security Program – which is the multilateral component of the U.S. government's Feed the Future Initiative – to support agricultural investments that reduce hunger and poverty in the poorest countries with real results. In Sierra Leone, for example, GAFSP financing has underwritten the delivery of improved extension services to farmers to help them boost yields in key staple crops. GAFSP has also financed the rehabilitation of 250 kilometers of rural roads in Togo to better connect farmers to local markets and has provided 18,000 farmers with better access to improved seed varieties and fertilizer.

Finally, this year, the United States will be making new commitments to the International Development Association of the World Bank (IDA), and the African Development Fund. These are the two largest sources of finances for the world's poorest countries, and their impact is enormous. For IDA, this is likely to be the last replenishment before countries like India graduate. With support from Congress, our investments have delivered real results on the ground. For example, IDA has helped 1.4 million people in Senegal to gain access to clean water and over 700,000 people Sierra Leone to have access to health care facilities. Once again, we have an opportunity to exert our leadership at these institutions and at the same time advance our moral commitment to ending global poverty and building a safer world.

Conclusion

Chairman Hensarling, Ranking Member Waters, and members of the committee: the IMF, the World Bank, and the MDBs have proven to be effective pillars of the international financial architecture. With U.S. leadership and backing from the Administration and Congress, I am confident they will continue to protect and support America's vital economic and national interests, today and into the future.

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